Self-employment for Unemployed Workers in Canada

Ging Wong, Fred Phelan, Bob Dugan and Zhengxi Lin

Introduction

Three separate analyses have recently been produced by the HRD Program Evaluation Branch examining the effectiveness of self-employment activities for unemployed workers. These examined the following issues:

- effectiveness of the Self-Employment Initiative (SEI) in achieving its objective of promoting labour market self-sufficiency through self-employment;
- trends and factors which influence self-employment participation for the Canadian labour force; and
- international evidence of success with self-employment programs.

The purpose of this brief is to present a summary and main conclusions of these studies.

Background and context

In Canada, the exploration of self-employment as an alternate re-employment option for unemployed workers began in 1987 when the Self-Employment Initiative (SEI) was introduced as part of the Community Futures program under the Canadian Jobs Strategy. The SEI option gave recipients of unemployment insurance and social assistance a chance to develop and operate new micro-businesses with the assistance of periodic income support payments. Its objective of "promoting labour market self-sufficiency through self-employment" suggested a two-fold purpose: (i) that the unemployed workers who create, own and operate new micro-business ventures work for themselves and are therefore "self-employed"; and (ii) that there is reduced dependency on UI or social assistance. While the primary purpose of micro-businesses is to provide remunerative employment for the owner-operators, they may provide jobs for other workers as well.

The idea of expanding employment opportunities by having unemployed workers create their own jobs was popular internationally and, by the mid-1980s, there were programs in more than 15 OECD countries.

In Canada, the Self-Employment Initiative (SEI) was evaluated in 1990 as an option under the Community Futures program. However, the evaluation lessons learned were limited to the impacts of entrepreneurial training on employability rather than on the program success of establishing and maintaining new small businesses while reducing reliance on UI and social assistance.

Against this backdrop, a new Canadian Self-Employment Assistance (SEA) program was initiated in June 1992, replacing the Self-Employment Initiative. This move created a self-employment program within the mandate of Unemployment Insurance Developmental Uses.

Methodology and data

The research on the SEI program was based on existing UI and taxation administrative data files. These were extensively mined to find out who participated in SEI and what could be determined about program outcomes. Specifically, the impact of SEI on improving earnings and on reducing UI dependency was examined.

The analysis of the gross flows into and out of self-employment in the Canadian labour force was based on the longitudinal data of the Labour Market Activity Survey (LMAS) for the years 1988-1990.

The international assessment of self-employment programs relied mainly on the evaluations of similar initiatives in England, France and the United States.

Key findings

SEI participation and impacts

The client profile covered SEI participants by year of participation, from 1987 to 1991. SEI participants were somewhat more likely to be males (59 per cent) than females (41 per cent). The majority (75 per cent) of participants fell into the prime age category (25-44). The linguistic profile of participants was similar to that of the Canadian labour force: 75 per cent indicated English as their first language and 25 per cent reported their first language was French. By designated group status, 6.6 per cent of participants were native Canadians and only a small fraction (3.3 per cent) reported disabilities. The 1987-1991 cohorts included 76.7 per cent UI claimants and 23.3 per cent provincial social assistance recipients (SARs).

We examined several aspects of the last job prior to SEI participation: job tenure; reason for job separation; occupation; and industry. The average tenure in their former job was 66.7 weeks, with most participants working one year or less in their previous job. Shortage of work was the major reason for separation from this previous job (50.6 per cent) with voluntary departure accounting for another 24 per cent. SEI participants were employed mainly in five general occupations: construction; clerical; service occupations; product fabricating, assembling and repairing; and sales. By major industry divisions, SEI participants had jobs mainly in the retailing sector, manufacturing, accommodation, food and beverage services, and government services.

Comparing the UI experience of each cohort for three years prior to SEI participation with their experience after participation, the analysis found that SEI participants were successful in reducing their reliance on UI. On average, 1988-1989 cohorts of SEI clients had 1.2 fewer claims after SEI compared to the average of the three years before SEI participation. SEI participants also experienced an average of 35.3 fewer paid UI weeks in the three years following participation as compared to a similar time period before SEI. The reduction in the number of UI claims established and the number of paid weeks received translated into a reduction in the level of UI benefits received by SEI clients following program participation.

This evidence suggests that SEI participation reduced the level of UI dependency, as measured by the number of UI claims established, the number of paid weeks, and the amount of benefits paid pre- and post-SEI. However, caution must be taken when interpreting the data. If an SEI client's business fails, they may be ineligible for UI benefits and may be forced to seek Social Assistance funding. Thus, the program goals may not be met if individuals who are ineligible for UI take up Social Assistance as a substitute. Unfortunately, reliable data on UI to Social Assistance transitions was not available for purposes of this analysis.

The analysis of real earnings changes for SEI participants compared pre- and post-SEI levels of earnings from two sources: (i) earnings from self-employment; and (ii) employment earnings. For comparison, a time series analysis was also made of real employment earnings for random samples of UI beneficiaries (UI only group) who established a benefit period commencement (BPC) in the same years as the SEI cohorts.

Generally, SEI participants were found to have a lower level of pre-program earnings than the UI-only group. While earnings dropped during both SEI and UI participation, the SEI group experienced a more severe drop in total earnings than the UI-only group. However, the SEI group experienced substantial growth in earnings by the second or third year following SEI participation, bringing them to similar or higher levels of earnings than observed for the general UI population.

Analysis of taxation administrative data indicated that the SEI cohorts had some self-employment income before participation in the SEI program, suggesting that the SEI group was predisposed to entrepreneurial activities before SEI. For those participants with previous self-employment experience, average self-employment earnings after SEI participation were found to be 66 per cent higher than for SEI participants with no earlier experience in self-employment. Similarly, mean employment earnings were on average 14 per cent higher for participants who had been self-employed before SEI. These observations raise the question as to whether this group of individuals would have engaged in self-employment activities even in the absence of the program. On the other hand, about 60 per cent of SEI participants reported no net self-employment earnings in any year after SEI started.

This finding may be interpreted in three ways: (i) these individuals did not engage in any self-employment activity; (ii) the zero earnings represent a break-even situation between business revenue and expenses; or (iii) zero earnings represent participants whose business failed in an earlier year but remained in the sample.

In order to obtain a measure of incrementality for the SEI program, the analysis of earnings was extended in the following way. First, a comparison (control) group of UI recipients who became self-employed without the benefit of SEI was selected by a cell-matching procedure. Second, differences-in-differences (DID) estimation was used to evaluate program incrementality.

The following estimates of SEI program impacts were obtained for the 1989 SEI cohort. The program impacts were calculated in terms of the effect of participation in the SEI program on the total annual earnings of participants, which were considered as the outcome measure in the present evaluation study.

- Overall, the SEI program had a positive impact on the total earnings of the participants. The total annual earnings of SEI participants increased, on average, by $3911 relative to the comparable group of non-participants.
- The program impacts were calculated for each province individually. These impacts were statistically significant for the provinces of Newfoundland, Quebec, and British Columbia. Participants in Newfoundland benefited the most, where the impact of SEI was estimated at an average of $9853 per participant. The estimates of earnings gain were $6975 for participants in B.C. and $5521 for those in Quebec.
- Participation in SEI had a positive and significant impact on both men and women. The estimated benefits were slightly higher for men, but the difference was small ($4005 for men and $3845 for women).
- The benefit of SEI participation was also estimated for men and women in two age groups: 1) people between 25-44 years of age and 2) people between 45-65 years of age. The estimated benefits were substantially higher for men in the older age group of 45-65 years than for the younger age group of 25-44 years. The same was true for women but the difference was much smaller. A higher success rate for participants in the older age group probably reflects greater payoffs in terms of experience and skills in managing self-employment.

The flow into and out of self-employment in Canada, 1988-1990

An empirical analysis of self-employment in Canada in the late 1980's was carried out, focusing on three major aspects: (i) the incidence of self-employment within the Canadian labour force; (ii) the transition to self-employment from unemployment and the role of unemployment insurance; and (iii) the survival of self-employment ventures. The data used for these analyses were the 1988-1990 longitudinal wave of the Labour Market Activity Survey (LMAS).

About 2.15 million Canadians were self-employed in each of 1988, 1989 and 1990, accounting for about 12 per cent of the working age (16-69) population or nearly 16 per cent of the total employed. Self- employed workers were concentrated in the primary, construction, sales and services industries; and in the managerial, sales, services, primary and processing occupations. A number of demographic factors were identified as affecting the probability of being self-employed: self-employment was concentrated in the prime age (25-54) group; the likelihood of self-employment was greater for university or higher education groups relative to other educational groups; and self-employment was nearly two times more likely for males than for females.

From the three years of LMAS longitudinal data, it was possible to identify those individuals who experienced unemployment as well as those in receipt of UI payments in one year and who made a transition to self-employment in the following year. The self-employment rate was more than twice as high among those who did not experience unemployment (13.4 per cent) as among those who experienced unemployment in the previous year (6.5 per cent). Among those who experienced unemployment in the previous year, the self-employment rate was 6.5 per cent and for those unemployed who were UI recipients, 6.5 per cent became self-employed.

One obvious measure of success of self-employment was the ability of the enterprise to survive. In the absence of any reliable data on the success of program participants to survive in self-employment, it is useful to examine the LMAS to determine the survival rate of self-employment ventures. The two-year overall survival rate (regardless of unemployment status in the previous year) was 88.7 and 83.6 per cent between 1988-1989 and 1989-1990 respectively. The three-year overall survival rate was 76.2 per cent between 1988-1990.

International assessments

Self-employment programs for the unemployed in other countries pre-date the Canadian experience by almost a decade. France began in 1979 on an

experimental basis to allow unemployed workers to capitalise their unemployment benefits to form start-up capital for new enterprise creation. The success of this pilot led to a national Chômeurs Créateurs program in 1980. Great Britain followed with the Enterprise Allowance Scheme that provided periodic payments of income support during the business start-up period. The self-employment payment models developed in these two countries have become the standards emulated by other countries.

- Survival rates three years after program participation ranged from 53 per cent (France) to 63 per cent (Britain).
- Of businesses surviving three years, about 25 per cent created jobs in addition to that of the proprietor. The rate of full-time job creation was 0.44 in Ireland (44 extra workers for 100 businesses) and 0.36 in Great Britain (36 extra workers for 100 businesses). The British evaluation reported that a further 28 workers per 100 businesses were employed on a part-time basis, for a total 0.64 job creation rate.

In the U.S., two experiments featuring random assignment into participant and control groups are still in progress. The French lump-sum payment model is being tested in a demonstration project in Washington State and the British periodic payment model is being tested in the State of Massachusetts.The interim estimates of program impacts from the Washington State SEED demonstration confirm the efficacy of self-employment as a re-employment option. The experimental results are as follows:

- SEED dramatically increased the likelihood of being self-employed, accelerated the timing of entry into self-employment, and increased earnings from self-employment;
- When self-employment and wage/salary outcomes were combined, the SEED demonstration had significantly positive impacts on employment outcomes and had no significant impacts on earnings outcomes;
- An analysis of SEED's impact on job creation revealed a significant impact on the employment of family members but no impact on the employment of others;
- Given these results, self-employment appears to be a viable policy tool for promoting the rapid re-employment of UI claimants. The question of cost-effectiveness, however, remains unanswered and will be addressed in the final report.

Conclusion

Separately and collectively, the three main lines of empirical evidence — the SEI experience, the Canadian gross flows in and out of self-employment, and the international assessments — are encouraging of self- employment for unemployed workers. However, this review of available data on self-employment indicates that there are substantial gaps in the available Canadian data that lead to many questions remaining unanswered. In order to answer pressing questions on program outcomes and cost-effectiveness, a full evaluation of Canadian self-employment is required.

Self-employment for Unemployed Workers in Canada by Ging Wong, Fred Phelan, Bob Dugan and Zhengxi Lin was published by Human Resources Development Canada as an Insurance Program evaluation report, March 1994.

Copies of the full report and further copies of this summary are available from:

Program Evaluation Branch
Strategic Policy
Human Resources Development Canada
Place de Ville, Tower B, 22nd Floor
112 Kent Street
Ottawa, Ontario K1A 0J9

Telephone: (613) 954-7709
Fax: (613) 954-0134